



Report To: Audit and Corporate Governance
Committee
Lead Officer: Executive Director (Corporate Services)

21 October 2016

Treasury Management Annual Report

Purpose

1. To report on the performance of the treasury management function for the period 1 April 2015 to 31 March 2016.
2. This is not a key decision but reporting to the Corporate Governance Committee is a requirement of the Council's Investment and Borrowing Strategy.

Recommendations

3. It is recommended that Corporate Governance Committee note the creditable performance of the treasury management function.

Reasons for Recommendations

4. The performance of the treasury management function should be reviewed to ensure reasonable returns are achieved commensurate with risk. This is achieved by being a member of a benchmarking group.

Background

5. The Borrowing and Investment Strategy approved by Council on 25 February 2016 requires an annual report to be presented to Corporate Governance Committee after the end of the financial year.

Considerations

6. Investments of £52.957 million were held by the Council at 31 March 2016, and included £50.257 million in fixed rate investments. Investments included £11.257 million to South Cambs Limited with a range of maturities up to 2021 with £5.96 million maturing at the end of October 2016, at which time a loan to the Company will be provided through Council borrowing from the Public Works Loans Board (PWLB) as agreed by Council (28 November 2013). A PWLB loan had previously been proposed for February 2016 but sufficient cash-flow balances and an increase in the approved counterparty investment limits enabled the Council to continue with investments.
7. The original estimate of interest forecast for the year 2015-16 of £590,500 was based on the expectation that the Council would borrow to on-lend to the company however,

cash flow balances have enabled the Council to continue with investments without a need to borrow thereby increasing interest receipts without debt interest payments.

	31 March 2016 £	31 March 2015 £
Local Authorities	0	2,000
Ermine Street Housing Clearing	11,257	4,072
Banks	20,500	22,500
Banks, other	2,500	2,500
Money Market Funds	2,650	870
Building Societies with assets:		
greater than £10,000 million	16,000	11,500
between £5,000 million and £10,000 million	0	0
between £1,500 million and £5,000 million	0	
Shares	50	50
	52,957	43,492

8. Investments achieved an in-year return of £0.740 million, £0.149 million more than estimated due in part to the higher rate of interest charged on investments with South Cambs Limited. Interest of £0.24m being received from South Cambs Limited and £0.502 from other fixed term deposit and money market funds.
9. The results for 2015-16 show that South Cambridgeshire achieved a return of 2.18% on combined investments (less than and more than 365 days) compared to 0.87% in 2014-15.
10. Money market funds achieved an average return during the year of 0.49% an improvement on the previous year. Sums held in money market funds are essentially overnight deposits to facilitate short term cash flow requirements.
11. During 2015-16 interest rates continued with a Bank of England base rate of 0.5% this has been followed, in August 2016, by the first rate cut since March 2009 falling to 0.25%. This trend has been reflected in market interest and money market rates, the yield curve remaining relatively unchanged during 2015-16 with rates ranging from 0.40% for 1 month to 1.9% for 5 years, since August these rates are 0.20% and 1.6% respectively.
12. The performance target is a greater return than average over a five-year rolling period. For 2015/16, a better than average return. Over the five-year period the target has been met.
13. In March 2012, following the introduction of the Housing Revenue Account Self Financing regime, the Council acquired debt of £205 million. The full sum was borrowed from the Public Works Loans Board at an average fixed rate of 3.5% as 41 individual loans with maturity dates between 2037 and 2057.

14. The Council's Borrowing and Investment Strategy states that the effective management and control of risk are the prime objectives of its treasury management activities. The specific risks in treasury management are:

- (a) **credit and counterparty risk**
The risk of failure by a counterparty to meet its contractual obligations to pay interest and repay principal: the Council's range of counterparties is restricted to UK banks, financial institutions approved by the Council and large building societies (all of which must have a satisfactory credit rating) and to public sector bodies.
- (b) **liquidity risk**
The risk that cash will not be available when it is needed: the Council has cash flow forecasts which are updated weekly, an overdraft facility with its bank and, as a last resort, can borrow on the open market or from the Public Works Loan Board.
- (c) **interest rate risk**
The risk of loss through adverse movements in interest rates: the Council mainly invests in fixed interest rate deposits so it accepts the risk of an opportunity cost that money is invested at fixed rates and market rates subsequently rise.
- (d) **exchange rate risk**
The risk of loss through adverse movements in exchange rates: the Council's Investment strategy restricts all treasury management transactions to £ sterling.
- (e) **refinancing risk**
The risk that maturing investments cannot be reinvested at favourable rates: the Council's investments for less than a year are made to match liabilities and for more than one year have a spread of maturity dates.
- (f) **legal and regulatory risk**
The risk of loss due to the Council or its counterparties failing to act in accordance with their legal powers and regulatory requirements: the Council only deals in simple investments and only deals with well recognised and perceived to be reliable counterparties.
- (g) **fraud, error and corruption**
The risk of loss through fraud, error and corruption; the Council has internal controls including segregation of duties, an internal audit function to evaluate those internal controls and fidelity guarantee insurance.
- (h) **market risk**
The risk of adverse fluctuations in the value of investments: the Council only invests in non-negotiable investments which are held to maturity and realised at face value.

Prudential Indicators

15. The Prudential Code for Capital Finance in Local Authorities came into effect from 1 April 2004, the objective being to provide a framework for capital programmes to ensure that:

- Capital expenditure plans are affordable;
- All external borrowing and other long term liabilities are within prudent and sustainable levels; and
- Treasury management decisions are taken in accordance with professional good practice.

The indicators are primarily to show whether a local authority is entering into a long term commitment which it may not be able to afford in the future. The Council's main long term commitment is the £205 million debt resulting from the Government's Housing Revenue Account Self Financing Reforms and the affordability and sustainability of this debt are addressed in the Housing Revenue Account business plan.

16. A key prudential indicator is the capital financing requirement, which is capital expenditure which has not been fully financed from a local authority's own resources in the year but has been covered by raising external or internal debt, the position at 31 March 2016 is shown below:

	31/03/2016 Estimate £ million	31/03/2016 Actual £ million	31/03/2017 Estimate £ million
General Fund	11.820	5.181	35.578
Housing Revenue Account	204.429	204.429	204.429
Total	216.249	209.610	240.007

The General Fund capital financing requirement fluctuates due to financing internally refuse and street cleaning vehicles, part of the purchase of wheeled bins and cash overdrawn on equity share repurchases, but this financing is then partly repaid over a period.

17. The actual financing of General Fund expenditure in 2015-16 is lower than the estimate due to external borrowing for on-lend to South Cambs Limited being deferred to 2016-17, funding requirements for the company in 2015-16 being covered from available Council cash balances.
18. One of the indicators of prudence is that net debt is not in excess of the capital financing requirement; this position is confirmed in the table below. External debt relates to the Housing Revenue Account Self Financing debt of £205 million, the Council set an external debt authorised limit for 2015/16 of £219.0 million.

	2015-16 Estimate £ million	2015-16 Actual £ million	2016-17 Estimate £ million
Borrowing	219.0	205.1	240.0
Investments	-40	-53	-53
Net debt	179.0	152.1	187.0

Options

19. Options for the investment of surplus funds will be limited in the future as it may be more beneficial to use such funds to reduce marginally and temporarily the £205 million debt arising from Housing Revenue Account Reform. Other options for any surplus funds include:
- (a) Out-sourcing; however, external managers usually require a minimum of £10 million for a period of at least three years and, with the reduction in capital receipts and other reserves, these requirements cannot be met;
 - (b) The Investment Strategy restricts the range of counterparties and weekly monitoring of credit ratings and bank financial strength ratings restricts this range even further. The range of counterparties could be extended but any additions would need to be subject to an assessment of risk as the successful identification, monitoring and control of risk is the Council's prime criteria for measuring the effectiveness of treasury management; and
 - (c) External treasury management consultants are used by many local authorities but there is no budget for this.

Implications

20. In the writing of this report, taking into account financial, legal, staffing, risk management, equality and diversity, climate change, community safety and any other key issues, the following implications have been considered: -

Financial

21. The in-house treasury management function achieved an average rate of 2.18% on combined investments. The average investment rate with South Cambs Limited being 3.35%.
22. The cost of the in-house investment function, excluding cash flow forecasting and planning and control, is estimated at £102 per million (£110 in 2014/15)..
23. The affordability of capital expenditure at 31 March 2016 has been affirmed by the prudential indicator for net debt which does not exceed the capital financing requirement.

Risk Management

24. As noted in this report.

Consultation responses (including from the Youth Council)

25. The Youth Council were not consulted.

Effect on Strategic Aims

26. This report has no direct implications for any of the Strategic Aims but any increase in interest received (commensurate with risk) may reduce the need for cuts in individual services and assist in the achievement of actions to support those aims.

Conclusion

27. The in-house treasury management has achieved a good performance in 2015/16 at a minimal cost.

Background Papers

Where [the Local Authorities \(Executive Arrangements\) \(Meetings and Access to Information\) \(England\) Regulations 2012](#) require documents to be open to inspection by members of the public, they must be available for inspection: -

- (a) at all reasonable hours at the offices of South Cambridgeshire District Council;
- (b) on the Council's website; and
- (c) in the case of documents to be available for inspection pursuant to regulation 15, on payment of a reasonable fee required by the Council by the person seeking to inspect the documents at the offices of South Cambridgeshire District Council.

CIPFA Treasury Management Benchmarking Club 2014 reports (confidential)

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